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INVESTMENTS BY FIDUCIARIES AS AFFECTED BY VIRGINIA STATUTES.

Trust funds, including in that term all monies in the hands of guardians, trustees and fiduciaries generally, form a considerable part of present day wealth. Their administration, and particularly their investment, is attended with very serious possible consequences to the fiduciaries. And yet it is believed that many well informed lawyers have overlooked the provisions of our Virginia Statutes as affecting possible liability for investments made in securities not specifically authorized by those statutes. And it would seem that a brief consideration of those statutes, in the light of the construction placed upon similar statutes in other states, might not be without some value as well as present interest, to the profession.

Of course where there is a proper instrument which definitely fixes the authority of the trustee or other fiduciary, that instrument is the guide and must control the question of liability. And this article is intended to deal only with such funds as are not controlled by their creating instrument but are subject to the general principles governing their administration.

Prior to 1916, the law was well settled in Virginia that a fiduciary in making investments of funds in his hands was held only to the exercise of a reasonable and honest discretion such as a reasonably prudent man would exercise in the management of his own affairs.

The rule was stated in *Elliott* v. *Carter,* 9 Gratt. 511, as follows:

> "Where a trustee has acted in good faith in the exercise of a fair discretion, and in the same manner in which he probably would have acted if the subject had been his own property and not held in trust, he ought not to be held responsible for any losses occurring in the management of the trust fund."

And the court further said in that case:

"It is doubtful whether a wise policy should require more of a trustee than that he should act in good faith and with the same prudence and discretion that he is accustomed to exercise in the management of his own affairs."

The following Virginia cases cite *Elliott* v. *Carter* with recurring approval, some of them incorporating the above quoted passages in the opinion:

Davis Comm'r *v.* Harman et als, 21 Gratt. 194,
Meyers' Ex'or. *v.* Zetelle, 21 Gratt. 733,
Hall *v.* Wall, 22 Gratt. 433,
Crouch *v.* Davis, 23 Gratt. 99,
Mills *v.* Mills, 28 Gratt. 479,
Thompson *v.* Brooke, 76 Va. 160,
Parsley *v.* Martin, 77 Va. 381,
Cooper *v.* Cooper, 77 Va. 204,
Elliott *v.* Howell, 78 Va. 307,
Wayland *v.* Crank, 79 Va. 609,
Jones *v.* Jones, 86 Va. 852.

Indeed there is no case found in our Reports which does not approve the rule as laid down in *Elliott* v. *Carter*. There are several cases in which fiduciaries were held liable for loss by investments in Confederate bonds, or through acceptance of Confederate currency, although other prudent business men were making such investments of their private fortunes; but these cases were based upon the Act of March 5, 1863, which specifically prescribes the conditions under which such investment could be made, and which had been disregarded in some particular.

Crickard's Ex'or. *v.* Crickard, 25 Gratt, 410,
Campbell's Ex'or. *v.* Campbell, 22 Gratt. 649,
Ammons' Adm'r. *v.* Wolfe, 26 Gratt. 621.
Carter *v.* Dulaney, 30 Gratt. 192,
Leake *v.* Leake, 75 Va. 799.

In these cases the court dealt with the particular statutory provisions dealing with Confederate securities and gave no consideration to the question of "good faith" or "fair discretion" which may have been exercised. They are, therefore, no ex-

ceptions to the unbroken line of cases which so clearly established the rule in Virginia as above announced.

But in 1916, Acts 1916, page 809, the General Assembly of Virginia enacted the following general statute:

> Section 2700-a. Executors, administrators, trustees and other fiduciaries may invest the funds held by them in a fiduciary capacity in the following securities, which are and shall be considered lawful investments:
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> (1) In the bonds issued under the act approved February fourteenth, eighteen hundred and eighty-two, commonly known as the Riddleberger bonds.
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> (2) In the stock or bonds or interest-bearing notes or obligations of the United States on those for which the faith of the United States is pledged to provide for the payment of the principal and interest, including the bonds of the District of Columbia.
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> (3) In the bonds of any county, city or town in Virginia, provided the amount of the bonds of such county, city or town, including the issue in which such investment is made does not exceed eighteen per centum of the assessed value of the real estate in the county, city or town subject to taxation as shown by the last preceding assessment for taxes, and provided the said bonds are the direct obligation of the county, city or town issuing the same, and for which the faith and credit of the issuing county, city or town is pledged.
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> (4) In bonds and negotiable notes secured by first mortgage or first deed of trust on unencumbered real estate in the State of Virginia, not to exceed eight per centum of the assessed value of said real estate and improvements. Before any loan is made upon real estate the lender shall be furnished with a satisfactory abstract of title, certificate of title or title insurance policy and a fire insurance policy in an old line company with loss if any made payable to the trustee as his interest may appear.

And at the Session of 1918 the statute was amended so as to include Federal Farm Loan Bonds in the list of securities in which investments are permitted.

The question, therefore, naturally arises: Does our present statute *restrict* all investments of trust funds to the prescribed list set forth therein; or is it merely permissive, setting forth those investments as to which no question can be raised, and

leaving investments in other securities to be determined under the rule of *Elliott* v. *Carter?*

There has been no decision of our court of last resort in which this statute has been under consideration. We must, therefore, look to other jurisdictions and authorities for such light as may be shed on the subject.

Sec. 6413 of the Revised Statutes of Ohio is as follows:

> "Executors, administrators, guardians and trustees may, when they have funds * * * invest the same in the certificates of indebtedness of this State or of the United States or in such other securities as may be approved by the court having control of the administration of the trust."

In the case of Willis *v.* Braucher (Ohio), 87 N. E. 185, this statute was considered. The trustee there had invested in bank stocks, but only after full and complete investigation and after consulting his attorney, the judge of the court and others. The court held that the terms of the trust under which he was acting authorized him to make the investment and that the statute did not apply. But in dealing with the statute the court said:

> "It is perhaps enough to say of this statute that it is permissive. *It provides for situations where the instrument constituting the trust does not otherwise provide.* (Italics ours). Undoubtedly it indicates a general policy; a policy of carefulness in the handling of trust funds; it points out a course free from risk, and affords a certain sure method by which the trustee may secure an affirmation of the legality of his investment in advance. So that, as a matter of prudence, resort to the methods indicated may be strongly commended; but the statute does not afford any special aid in determining the question involved in the case at bar, *unless it be ascertained that the will gives no added authority to the trustee.*" (Italics ours.)

It would thus appear that, while the Ohio Court was not required to so decide in that case, and did not specifically so hold, it would decide in a case presenting the question squarely that a fiduciary could not invest in securities not listed in the statute where the creating instrument did not itself give authority for such investment.

The State of Illinois also has a statute which provides that where the instrument creating the trust fund does not otherwise direct, investments of trust funds by trustees may be made in certain designated securities. In the case of Merchants', etc., Co. *v.* Northern Trust Company (Ill.), 95 N. E. 59, which was brought for the purpose of construing the will of Marshall Field, it was held that the will itself gave authority to the trustees to make investments in other securities than those enumerated in the statute. But the court said, in referring to the Illinois Statute:

> "Such statutes are generally permissive rather than mandatory. They are intended to provide for situations where the instrument constituting the trust does not otherwise provide."

And the court cites with approval the Ohio case of Willis *v.* Braucher, which, it will be noted, also dealt with an instrument which *itself* gave authority for investments in other securities than those enumerated by the Ohio Statute.

In Wisconsin the rule had been clearly established in Simmons *v.* Oliver, 74 Wis. 633, that a trustee could not lawfully invest trust funds in other than government securities and real estate mortgages, regardless of the prudence and care exercised in the investment made in other securities. Subsequently to this decision the legislature enacted a statute providing that investments of trust funds might be made in government and real estate securities where the creating instrument did not specifically direct or permit other investments.

This statute was construed to be a legislative approval of the rule of Simmons *v.* Oliver and exclusive in its limitation of investments where the trustee was not given larger discretion in the appointive instrument.

In the case of In re Allis' Estate (Wis.), 101 N. W. 365, the court said:

> "The language 'may invest trust funds in governmental and real estate securities' recognizes that the law of the state sanctions investments of trust funds according to the rule laid down in Simmons *v.* Oliver; and we are led to believe that the legislature enacted this chapter in recogni-

tion of the law so declared. * * * In view of this legislative and judicial declaration on the subject, we perceive no sufficient grounds for changing or modifying the established rule controlling trustees making investments of trust funds."

The Kentucky statute provides that trust funds may be invested 'in certain designated securities "or in such other interest bearing or dividend paying securities as are regarded by prudent business men as safe investments. * * * But such funds shall not be invested in the bonds or securities of any railroad or other corporation, unless such railroad or other corporation has been in operation more than ten years and during that time has not defaulted in the payment of principal and interest on its bonded debt."

In Robertson *v.* Robertson's Trustee (Ky.), 113 S. W. 138, a case was presented in which the trustee had invested the trust funds in the stock of a bank which had been in existence only one year. The trustee had acted in good faith, and the stock was worth as much, or more, than he paid for it. He contended that the investment was authorized by the clause of the statute which permitted investments in "such other interest bearing or dividend paying securities as are regarded by prudent business men as safe investments."

The court refused to sustain this contention and held that investments could be made in the stocks of banks only after they had been in existence for ten years, saying:

"We are not willing, on the one hand, to widen by interpretation the field for the investment of trust funds, without also by interpretation holding fast to the safeguards which the legislature has thrown around such investments. * * * It seems to us that assuming for the purposes of this case that bank stock is legitimate property for the investment of trust funds under the permissive part of the statute, it is also included in the inhibitory part and that before a trustee is permitted to invest the funds of his cestui que trust in stock of private corporations, these must have fulfilled the requirements of the statute as to the time of their existence."

It is true the court in this case dealt with a definitely restrictive clause of the statute; but it would seem to be in line

with the cases cited above in holding investments strictly to those securities listed in the statutes.

In Connecticut, however, a different conclusion was reached in construing a statute of that state which is similar in its general terms to those of Ohio and Illinois above referred to. Clark *v.* Beers, 61 Conn. 87. The court cited no authorities in the brief opinion handed down but did deal squarely with the question here under consideration. The court said:

> "We do not construe the provisions of Sec. 495 of the General Statutes as mandatory and as depriving trustees of all discretion as to investments. If they invest in the securities expressly allowed by the statute they will, except under very extraordinary circumstances, be protected no matter how the investment may result. Acting within the express provisions of the statute would be, of itself, proof of good faith and sound discretion. All investments other than those named in the statutes must be justified when occasion arises, under the rigid rules applicable to investments made by trustees upon their own judgment."

This decision was rendered long prior to those of Ohio, Illinois and Wisconsin, above referred to, and, although not mentioned in those later cases, must be considered as disapproved by them since the conclusions reached therein are so directly contrary to that of the Connecticut Court.

And in Lamar *v.* Micou, 112 U. S. 452, a Georgia Statute, authorizing trust funds to be invested in certain designated securities was held, adopting the rule laid down in that State by cases cited, not to be compulsory. And a fiduciary was protected against loss arising from an investment which he had made in good faith and in the exercise of reasonable prudence.

The few cases referred to are all that a fairly diligent search for authorities has disclosed. And it would seem unwise to say more than that the reasonable weight of authority appears to be against the legality of investments in securities other than those listed in the statute. It is true that the Ohio and Illinois decisions referred to were not required to meet the question squarely, and the Wisconsin decision merely reaffirmed a rule which the statute was held to have embodied in legislative declaration. But the language of the opinions leaves

no doubt as to what the result would be in cases directly presenting the question for specific determination.

The weight of reason seems clearly to favor the rule holding the statutes to be exclusive. They point so safe a course and one so easy to follow that there would appear to be no undue hardship in holding a fiduciary responsible who elected to follow a different course.

It is true that Judge Lee said, in Elliott *v.* Carter, supra:

> "A trust is an office necessary in the concerns between man and man, and which if faithfully discharged is attended with no small degree of trouble and anxiety and it is an act of kindness in any one to accept it. To add hazard or risk to that trouble and to subject a trustee to losses which he could not foresee would be a manifest hardship and would be deterring every one from accepting so necessary an office."

But the answer is plain, simple and direct. The statute is your chart. Follow it and you cannot go wrong.

It is also true that the opinion in Elliott *v.* Carter said:

> "It is doubtful whether a wise policy should ever require more of a trustee than that he should act in good faith and with the same prudence and discretion that he is accustomed to exercise in the management of his own affairs."

But has not the General Assembly of Virginia in enacting the statute now in force, adopted a more restricted rule and for the specific purpose of changing the policy announced in Elliott *v.* Carter? What need for a statute unless such a purpose were in view? The rule was well settled in Virginia prior to the enactment of 1916; and unless it be intended as restrictive it would be of little or no use except in pointing out permissive instruments as to the character of which there had never been any doubt.

The statute in question includes practically all forms of investments other than corporate stocks and by omitting these investments, which in but few states have ever been regarded as proper for trust funds, weight is given to the view that the

statute was intended to be restrictive. The rule as to corporate stocks is stated in 39 Cyc:

> "Except where authorized by express provisions in the instrument creating the trust or statutory provisions in regard to the character of the securities in which trust funds may properly be invested, the general rule is that a trustee cannot invest such funds in the stocks, bonds or other securities of private business corporations."

The question is not without its difficulties which might easily be settled by appropriate legislation. But in the meantime it may be safely asserted that a fiduciary would be running a most serious and unnecessary risk in making investments in securities other than those listed in the statute.

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